



PHILLIP SECURITIES PTE LTD

Unit Trust – Asset Class Update

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February May Be The Same As January After All

Executive Summary

Equities – Equities in China, India and Indonesia suffered substantial losses while Russia outperformed. Information Technology sector may trend lower in the near term.

Commodities – Oil prices likely to remain below US\$100/bbl. in the near term; Gold ETF holdings hit 4-month low as gold prices retreated.

Fixed income – The periphery European debt uncertainty prevails though minimal chances of any outright default; Treasury yields likely to trade higher in the medium term, adding downward pressure on bond prices.

Equities – Inflation Fear in Asia Starts Spreading

China's economy grew 10.3% last year, the fastest pace in three years, raising fears that the Chinese government would hike interest rates again to slow its growth and fend off inflation. Energy stocks and emerging markets stocks fell on China's economic report and the Shanghai Composite lost nearly 6.5% so far over the 1-month period (See Table 1 below). We feel that investment fund flows is rotating away from challenges and concerns, such as rising inflation within China, Indonesia and India. Unrest in Egypt was spurred by a nationwide uprising against President Hosni Mubarak and this further dampened the investment mood.

Overall, major global indices were slightly up over the one month period and we continue to see outperformance coming from the Russia equities, up 28.4% over the 6-month period so far. We maintain that global equities will continue to perform well over the next month period and through the first quarter of this year itself. Nevertheless, investors should manage their risks accordingly, and look for the opportunities in the aftermath of any near-term correction move.

Table 1: Selected Equity Stock Market Index Returns

Country	Index	Jan. 21	1-mth % gain/loss	3-mth % gain/loss	6-mth % gain/loss	52 week High	52 week Low
Russia	Micex Index	1740.08	3.96 ▲	13.87 ▲	28.44 ▲	1788.74	1194.96
Hong Kong	Hang Seng Index	23876.86	3.84 ▲	0.96 ▲	16.55 ▲	24988.57	18971.52
Europe	Euro Stoxx 50 Pr	2940.10	2.19 ▲	2.01 ▲	11.39 ▲	3027.14	2448.10
United States	S&P 500 Index	1280.26	2.05 ▲	8.47 ▲	19.70 ▲	1296.06	1010.91
Brazil	Brazil Bovespa Index	69561.53	1.97 ▲	-0.13 ▼	7.89 ▲	73103.28	57633.90
Singapore	Straits Times Index	3184.84	1.43 ▲	0.67 ▲	8.84 ▲	3313.61	2648.15
Australia	S&P/ASX 200 Index	4755.70	-0.34 ▼	2.87 ▲	7.77 ▲	5025.10	4175.70
India	BSE Sensex 30 Index	18980.33	-5.38 ▼	-6.32 ▼	5.58 ▲	21108.64	15651.99
China	Shanghai SE Composite	2715.29	-6.50 ▼	-8.99 ▼	7.10 ▲	3186.72	2319.74
Indonesia	Jakarta Composite Index	3363.47	-7.53 ▼	-6.26 ▼	11.62 ▲	3789.47	2431.84

Major global equities were mostly up on a monthly basis. China, India and Indonesia equities suffered substantial losses.

Source: Bloomberg, as of 21 Jan 2011



Wall Street versus Main Street – Separating Them

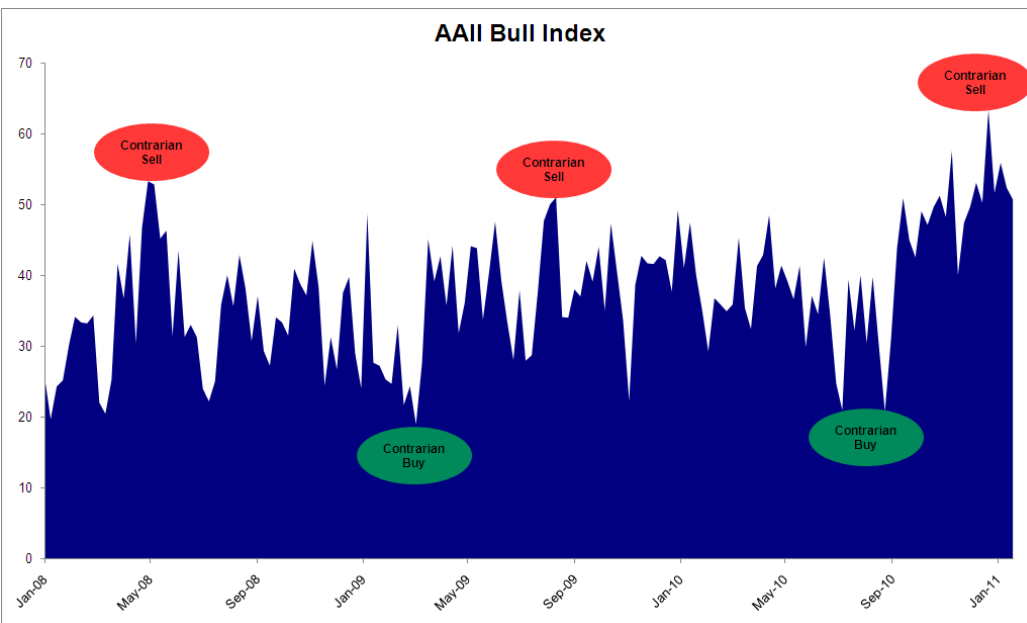
There is an increasing disparity between the performance of the US economy and the US stock market performance. The US economy is still enduring sluggish employment and housing while US stocks continue making new highs. Investors were focusing less on what should be good for the economy (job growth, fair market regulations and housing etc) while targeting higher companies' profits (no matter their sources).

From the earnings perspective, it was estimated that more than 40% of the S&P 500 company earnings came from overseas. Thus, we believe that US companies are more interconnected with today's global macroeconomic health. On the other hand, despite the US initial jobless claims fell more than 100,000 since August 2010, unemployment rate remains high. Although domestic unemployment continue to be a drag on the US economy at the moment, we view that US companies' earnings will not be affected to a great extent (a similar scenario as compared to the 2003 recovery).

Nevertheless, we believe that there may be a possible correction/pullback to balance out the overbought indicators. The AAll Sentiment Survey measures the expectations that stock prices will rise over the next six months. As of the most recent reading, the level of bullishness read at 50.7%, a five-week low (See Chart 1 below). The level of optimism remains more than one standard deviation above its historic average of 39%, a sign that it remains at high levels. We view this as a contrarian sell signal and the equity rally may be not undeterred for long.

No doubt, the Main Street guy may be still struggling to land a job. On the hindsight, the Wall Street banker/trader looks ready to cash in on the recent rally.

Chart 1: AAll Bull Index Remain at High Levels



The AAll bull index is reflecting the bullish sentiment at the moment, next wave of technical correction may be waiting in line.

Source: Bloomberg, as of 20 Jan 2011



Near-Term Risks in Information Technology Sector – US Perspective

We view that although recent earnings in the US technology sector have been picking up well and impressive, the US technology sector may not be an attractive sector to be in at the moment. Broadly speaking, the global technology sector can be broken down into the semiconductors, networking, computer hardware and software categories and we will look into them as follows:

Semiconductors (up 38.3% since Jul-2010) – We feel that both the LEDs and cloud computing stocks had their big moves to the upside but the earnings are not validating the moves. There may also be a potential change in consumer behavior as individuals are shunning away from PCs and turning to smart phones and tablets, like the Apple iPad, resulting in market cannibalisation on the chipmakers.

Networking (up 40.5% since Jul-2010) – On the S&P North American Technology Multimedia Networking Index, we feel that support is at 132, which would be approximately 10% off the recent highs. It will be a challenge for companies like Cisco to sustain its double digit earnings growth in 2011 (Cisco's earnings rose 27% in fiscal 2010, from US\$6.13 billion to US\$7.77 billion). We expect earnings growth in the networking space to moderate in 2011.

Computer hardware (up 27.0% since Jul-2010) – May be falling victim to the cannibalisation effect in the wake of the tablet euphoria as described above. For instance, Seagate recently reported sales fell 10% and the outlook is for more of the same next quarter. The demand in Asia was down, which had been a theme in several areas of the technology sector.

Software (up 30.8% since Jul-2010) – Perhaps the only bright spot within the technology sector. Software giants such as Microsoft are moving to acquiring other tech companies, entering growing markets and acquiring new technologies.

The technology may be a mature market where you have to think in terms of long-term returns. In fact, some parts of the sector may be experiencing growth pains. Though the longer term view for the sector remains positive on the back of strong cash flows and innovation capabilities, market may have priced in most of the positives and valuations are rich at the moment (See Table 2 below).

Table 2: Valuation of Technology Sector is Rich

Name	Jan. 24	Dividend Yield (1Yr)	Price to Book	Forward PE	Current PE
S&P North American Tech Semiconductors Index	239.98	1.08	3.10	13.60	16.78
S&P North American Tech Multimedia Networking Index	142.19	0.44	2.74	17.56	24.94
S&P North American Tech Hardware Index	484.81	0.23	2.55	13.31	16.40
S&P North American Tech Software Index	244.62	0.32	3.99	19.34	28.90
S&P North American Tech Index	253.57	0.79	3.57	14.26	17.33
Nasdaq Composite Index	2689.54	0.94	2.95	17.24	33.56
MSCI World Information Tech	91.73	1.06	3.07	14.07	16.82
US S&P 500 Index	1283.35	1.84	2.25	13.42	15.64

Source: Bloomberg, as of 24 Jan 2011

Technology sector on the whole is less than attractive as compared to the broad market index at the moment.



Commodities – Positioning For The Next Move Up

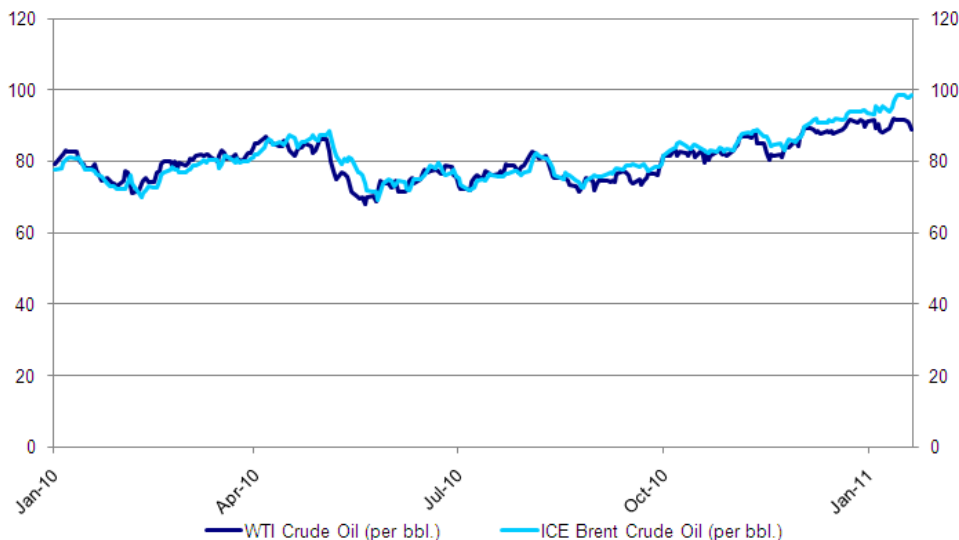
The rise in commodities so far can be attributed to the strong demand surge from developing countries on the back of unprecedented loose monetary policy at the US. From a near term perspective, the flooding in Australia may add further pressure to the commodity-driven inflation picture. Coking coal is a key ingredient in steel production and the flooding in Queensland has temporarily suspended production at mines which amounts to an estimated 40% of world supply. Risk of overheating are emerging and some developing nations are already putting measures in place to fight inflationary pressure. Food inflation may soon become a major problem for these developing countries and governments may have little tools to control the continual rise in food prices. Overall, we believe that the upward pressure on commodity prices appears to have staying power for now.

On the energy front, many advocates are concerned about the impact of increasing oil prices on the global economy. According to the Financial Times, the ratio of countries' oil import bills to GDP, a key measure of the cost of oil prices on economies, is close to levels last seen during the financial crisis in 2008. Accordingly, if oil prices remain above US\$90/bbl for the rest of this year then the ratio for the European Union will be 2.1%— close to the 2.2% level it reached in 2008. High energy prices may push US into a deflationary environment. US consume more than 370 million gallons of gas per day, each dollar rise in gas prices, if sustained, means US\$2.6 billion a week must be diverted toward the gas pump and away from other spending.

As mentioned in our earlier report, we maintain the view that any upside on crude prices will be limited below the US\$100/bbl. mark. The supply-demand balance is likely to stay benign in 2011 and that macroeconomic picture is likely to dominate energy prices as a whole. (For more information please refer to Investment Outlook 2011 report).

Chart 2: Crude Oil Prices Likely to Stay Below US\$100/bbl.

Crude Oil Prices



Crude oil prices had been trending up since Sept-2010, likely to stay below the US\$100/bbl. mark.

Source: Bloomberg, as of 20 Jan 2011



Gold – ETF Holdings Hit Four-Month Low

In the aftermath of the 2008 crisis meltdown, gold had managed to remain broadly well-supported throughout. In fact, many saw the gold commodity as an attractive store of value and its price had since doubled from the US\$700/Oz. level back in 2008. However, the two-year rally in gold may take a dive over the near term before we see new highs again.

The reversal in investment demand is hurting gold prices at the moment. It appeared that investment demand was the main driver for the metal's spectacular performance in 2009 and 2010 (See Chart 3 below). Exchange-traded funds (ETFs) have become an increasingly attractive vehicle for gold exposure given their ease of use compared to physically buying bullion. The gold ETF investment took a backseat during the week of 14 Jan 2010. The total known holdings snapped the rising trend carved out through the fourth quarter of last year to drop to the lowest since mid-Sept 2010. Gold investors exited their positions on the back of improving US economic data and a back-slide into recession is now remotely unlikely.

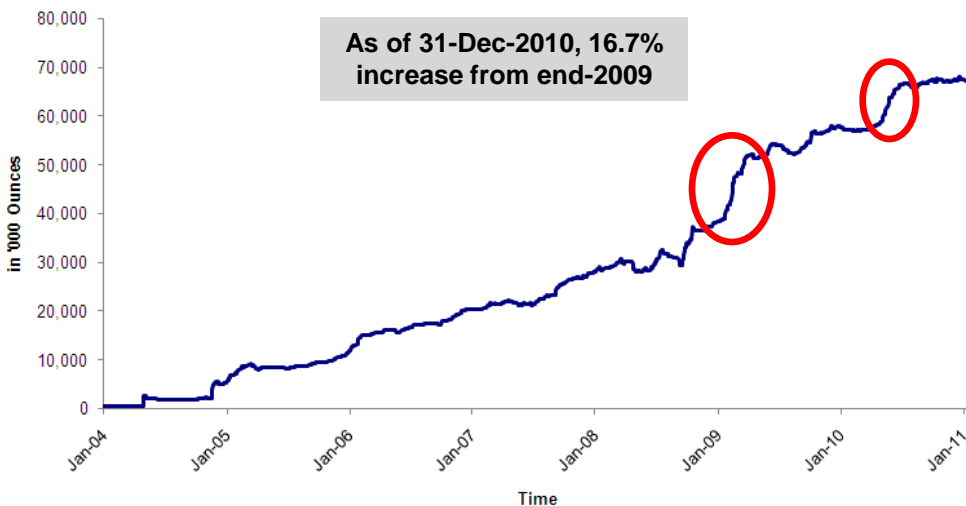
However, investors should not overlook the many headwinds that are still in the pipeline. Overheating concerns in China and the lingering debt crisis in the Eurozone are likely to prolong the global recovery period ahead. At the same time, demand for gold may be surrounded by the fear of inflation over the long term. The question remains whether central banks are able to mop up the flood of liquidity created through record-low interest rates and quantitative easing. This will see prices soar on a global scale, debasing paper currencies and making a hard asset store of value like gold a very attractive alternative.

In the short term, gold may yet be susceptible to a long-overdue correction lower. We are positive on the long term appeal of gold as a hard asset investment and the upward trend in gold price remains intact.

Chart 3: Investment Demand for Gold Tapering Off Slightly

Gold Exchange Traded Funds Demand

As of 31-Dec-2010, 16.7% increase from end-2009



The bullish performance of gold prices since 2009 was driven by an exponential increase in investment demand on the metal.

Source: Bloomberg, as of 20 Jan 2011



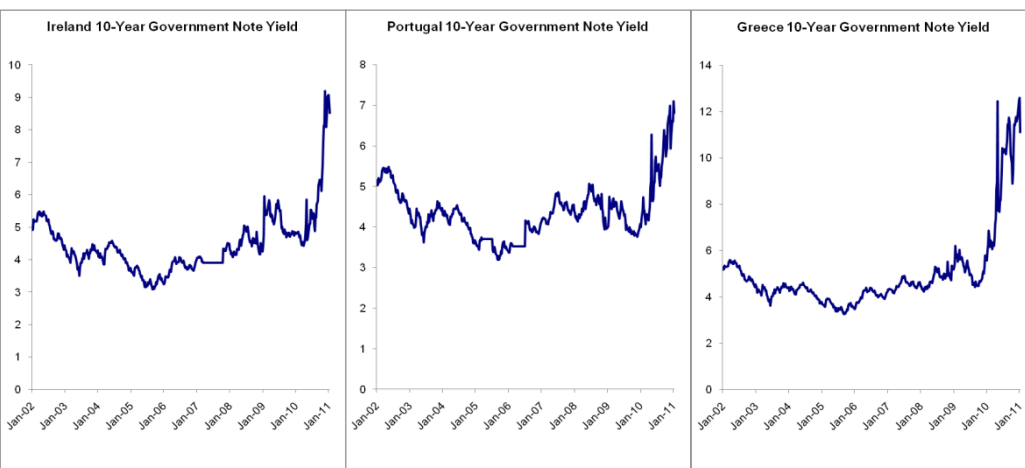
Fixed Income – Yields May Have Moved Too Much Too Fast

Since the start of 2010, the sovereign debt woes in Eurozone escalated as the days passed. The result was rising costs of insuring the region's debts (See Chart 4 below). Countries like Ireland, Greece, Portugal and Spain, once considered safe sovereigns, are more likely to default than Iraq, according to CMA Datavision's latest report (See Table 3 on the next page). The surge over the last two months puts the Eurozone crisis into context. While the presumption was that the monetary union remains one of the world's most stable markets, investors now view it as one of the most dangerous debt markets in the world. CMA's list is ranked by CPD, or cumulative probability of default. Though we view an outright default on European sovereign debts as an unlikely scenario, the outlook is certainly less than positive at the moment.

In fact, individual PIIGS bond rates spiked as large bond sales approach. One key uncertainty had been the reluctance of German Finance Minister Wolfgang Schauble's to expand the EFSF, EU's bailout fund. The speculators remain skeptical that the EU can backstop Spain (the next BIG thing) and fluctuating sentiment about the plenty EU trouble spots prevails.

On the Treasuries, it had been a challenge on the Fed Reserve to bring down the yields across maturities. An upward shift in the yield curve since the time of the Fed Reserve's QE2 announcement was observed (See Chart 5 on the next page). Adding to the woes, the average interest rate for 30-Yr and 15-Yr fixed rate mortgages and 1-Yr ARMs have been trending up for about twelve weeks now and coincidentally somewhat in-line with the Fed Reserve making QE2 official. It appeared that the actual implementation of the QE2 measures is not currently working to force the rates down any lower. We continue to advocate cautious ahead on the Treasuries and are less than positive on the overall sovereign debt space.

Chart 4: Surging Bond Yields on Periphery European Nations



The 10-year government yields signal more headwinds ahead for the periphery European nations.

Source: Bloomberg, as of 19 Jan 2011



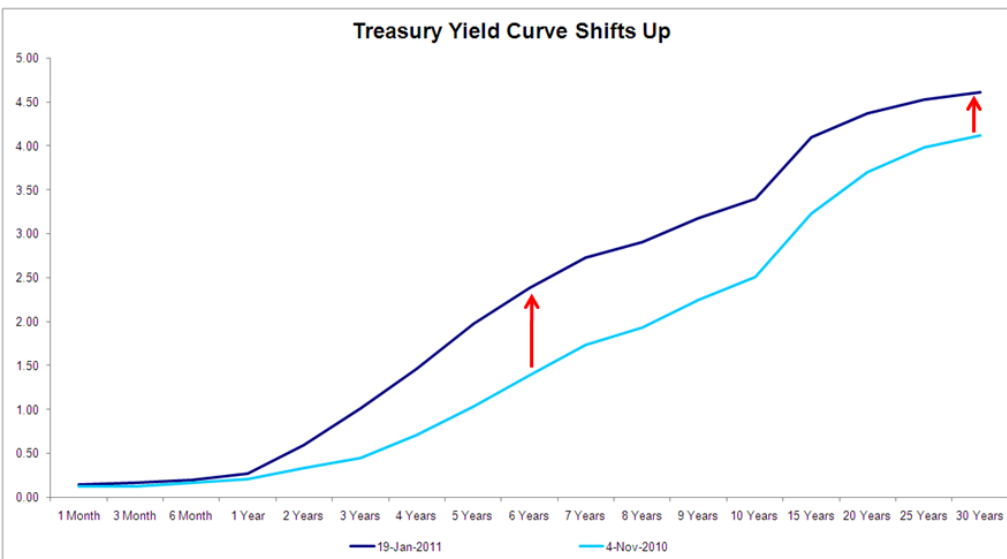
Table 3: Countries Most Likely To Default

Countries	Cumulative Probability of Default	Current 5-year Mid CDS (bps)	CMA Implied Rating (Dec 31)	CMA Implied Rating (Q3)
Greece	58.80%	1026.5	CCC- ▼	CCC+
Venezuela	51.40%	1009.6	CCC+ ▲	CCC
Ireland	41.20%	619.2	B---	B
Portugal	35.90%	497.3	B ▼	B+
Argentina	35.40%	602.4	B ▲	B-
Ukraine	30.60%	509.5	B+ ▲	B
Spain	27.70%	347.7	BB- ▼	BB
Dubai	25.50%	417.6	BB- ▼	B+
Hungary	23.60%	378	BB- ▼	BB
Iraq	23.10%	366.1	BB- ▼	B+

Source: CMA Datavision, as of Jan 2011

Country's like Ireland, Greece, Portugal and Spain, once considered safe sovereigns, are more likely to default than Iraq, according to CMA Datavision's latest report.

Chart 5: Shift in US Treasury Yield Curve Upwards



Source: Bloomberg, as of 19 Jan 2011

A comparison of the yield curve at the time of the Fed's QE2 announcement and the latest curve shows an increase in yields across maturities.



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